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EXTERNAL DEBT CRISIS AND DEVELOPMENT

Recent experience under the international debt strategy

Report of the Secretary-General

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I. INTRODUCTION

1. The international debt crisis of the developing countries has reached its tenth year, measured from August 1982 when Mexico became unable to service its commercial bank debt. On this anniversary, it is particularly noteworthy that several important developments in international debt policy have taken place over the past 12 months. First, perceptions in the international financial markets of the creditworthiness of the major heavily indebted countries improved significantly, as borrowers in some of these countries returned to the market, albeit paying significant interest premiums. Second, more countries negotiated debt and debt-service reduction agreements with their bank creditors; these are meant to be the final of several rounds of bank negotiations. Third, a new and more concessional set of terms was adopted in the Paris Club - the debt-restructuring forum for official, industrial-country creditors, which are being applied to low-income, heavily-indebted countries undertaking economic adjustment programmes. What remains to be seen is whether the new agreements will in fact eliminate the debt overhang, whether a sufficient number of countries will be able to take advantage of them, whether the financial improvements will be solidified in renewed, sustainable and sustained flows of external finance to the heavily indebted countries and, finally, whether the affected economies will recover from the lost decade of debt crisis.

2. The major developments of the past year follow several improvements in the policies governing the international treatment of debt, which were noted by the General Assembly in its resolution 46/148 of 18 December 1991. In that resolution, the Assembly, after reviewing the international debt situation of the developing countries as described in the report of the Secretary-General (A/46/415) and in the debate under agenda item 81, entitled "External debt crisis and development", expressed a deepening of the international consensus on policy priorities and concerns for overcoming foreign debt crises in developing countries. The developing country debt situation continues to be monitored in view of the role of debt crises, inter alia, in inhibiting necessary increases in investment and in prolonging the strains on social and political stability from protracted economic adjustment processes. This report thus examines recent policies in action in the private and public sphere of external debt and updates the Secretary-General's report of 1991. 1/

II. CURRENT SITUATION IN HEAVILY INDEBTED DEVELOPING COUNTRIES

3. After a decade of crisis, disappointment, and stagnation, the heavily indebted developing countries are anxious to leave behind the debt-related problems of the 1980s and return to the essential process of economic and social development. Where an unsustainable growth in foreign borrowing originated in unsustainable macroeconomic policies, this has meant facing up to the need for corrective policies. Where the growth of debt was in reaction to inflexible and declining export sectors, the need for structural adjustment

to promote competitive production of tradable goods and services has had to be accepted. By the same token, after adverse international economic developments first made incipient debt crises painfully visible and then demonstrated their nature to be insolvency rather than illiquidity, the creditor community has had to respond with increasing degrees of debt relief.

4. While some Asian economies led the adjustment process in the 1980s, several Latin American countries have now begun to show some of the fruits of adjustments begun in the 1980s. A major external support to this process has come recently in new financial inflows arranged by both domestic and foreign business communities, encouraged in some measure by new debt agreements, but also by a fortuitous drop in United States dollar interest rates relative to high Latin American rates. In Africa, where the structural difficulties have been deeper, the payoffs have been slowest to emerge and the overall prognosis remains the most difficult. In none of the recently adjusting, heavily indebted countries, however, can it be said that the rate of capital formation has surged or that the economy has returned to a higher long-run growth path. That the economic and financial conditions for such developments are being set in several countries is a source of optimism. That the period of adjustment, slow economic growth, intensified social inequities and political tensions might be further protracted in other countries remains cause for concern.

A. The state of indebtedness

5. The total stock of external debt of the capital-importing developing countries 2/ was about $1,260 billion at the end of 1991, virtually the same as in 1990 (see table 1). The net lending flow was for the most part offset by debt conversion, debt cancellation, clearance of arrears and exchange-rate valuation changes. The debt owed to official creditors continued to increase its share of total debt, reaching 46 per cent in 1991. It had been only 35 per cent in 1981. The debt owed to the private sector has not only been falling as a share of the total, but the level itself has been declining steadily since the peak in 1987.

6. Although the total amount of debt in dollar terms has remained at about the same level since 1987, it fell from 50 per cent of GNP that year to 36 per cent in 1991. The debt-to-export ratio also fell in this period; it had peaked in 1986 at 200 per cent and reached 133 per cent in 1991.

7. Africa's total debt decreased slightly, reflecting in part a large write-off of the debt owed by Egypt to official creditors. As a ratio to GNP, Africa's debt is none the less the highest among the major developing country regions, although the share of export earnings needed for debt servicing lies below that for Latin America and the Caribbean (see figure 1). Debt-servicing payments by sub-Saharan African countries fell slightly 3/ but the debt service-to-export ratio did not decline, owing to poor export earnings as commodity export prices fell. This interrupted the trend since 1987 of declining debt-servicing ratios, which had been partly due to increases in export volumes, but also reflected the region's continued severe difficulties in meeting debt-servicing obligations.

Table 1. Debt and debt servicing of the capital-importing developing countries, 1981-1991

(Billions of United States dollars)

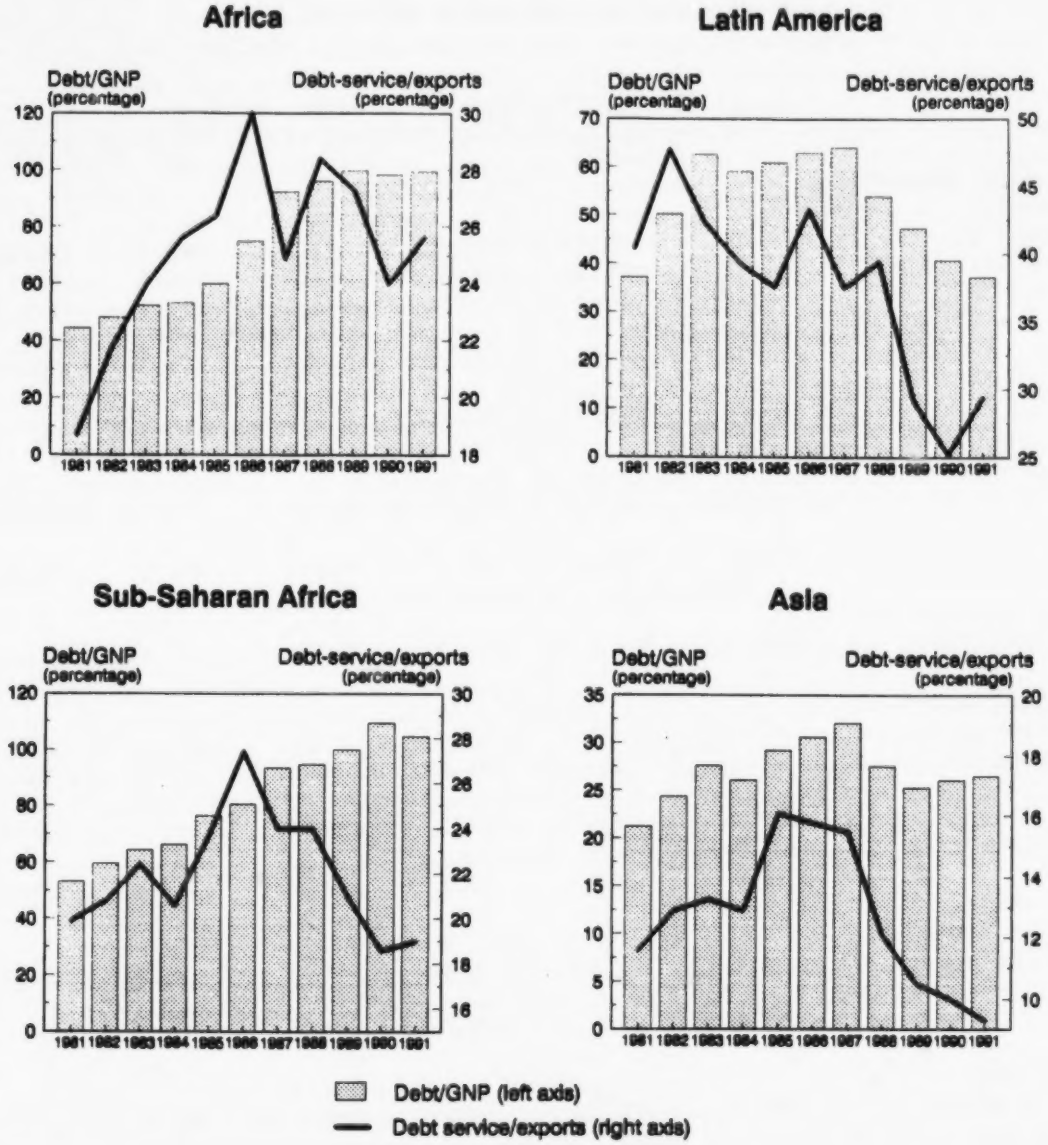
	1981	1987	1988	1989	1990	1991 a/
Total debt outstanding						
Long-term						
Official	242.4	530.4	529.2	548.1	559.3	573.5
Private	306.1	536.5	521.2	501.9	496.8	487.5
Short-term	148.9	144.3	150.8	165.4	194.4	198.9
Total	697.4	1 211.2	1 201.2	1 215.4	1 250.5	1 259.9
of which,						
Africa	126.9	251.3	255.8	226.0	277.7	274.7
of which, sub-Saharan Africa b/	45.8	100.0	101.0	105.4	118.7	121.2
Asia	204.2	393.3	396.7	404.9	423.1	440.1
Latin America and the Caribbean	317.2	475.0	457.5	452.1	447.7	444.9
Total debt servicing						
Interest payments	60.3	63.2	73.1	66.4	63.8	71.3
Principal repaid	46.6	73.9	74.2	71.5	75.7	76.3
Total	106.9	137.1	147.3	137.9	139.5	147.6
of which,						
Africa	15.6	19.2	22.7	23.5	25.4	27.4
of which, sub-Saharan Africa b/	5.4	7.7	7.9	7.5	7.1	6.6
Asia	27.7	58.8	55.5	54.7	56.8	58.3
Latin America and the Caribbean	56.3	47.0	55.2	45.9	42.5	48.1

Source: United Nations, World Economic Survey, 1992.

a/ Preliminary.

b/ Excluding Nigeria and South Africa.

Figure 1. Debt indicators of major developing regions, 1981-1991 a/



Source: United Nations, World Economic Survey, 1992.

a/ Excluding major oil-exporting countries of the Middle East and Libyan Arab Jamahiriya; sub-Saharan Africa excludes Nigeria.

8. As in Africa as a whole, the debt of Latin America fell slightly, while debt servicing rose more than $5 billion, mainly because of certain payments of interest arrears. The fall in Latin America's debt reflected various debt negotiations concluded in 1990 and debt conversion schemes. A notable case of the latter was in Argentina, where proceeds from the privatization of telephone and airline companies eliminated $7 billion of its debt in 1991. The debt stock of Asian countries grew, reflecting their continued market access and use of official credit. But Asia's increase in its debt stock was balanced by its strong export performance, causing a further decline of the Asian debt-servicing ratio.

9. On a quantitatively smaller scale, more cases of debt-for-nature swaps have been taking place as interest and understanding rise on environmental issues and the swap mechanism. 4/ In general, debt is either bought or donated to non-governmental, non-profit organizations working for conservation in developing countries. The debt is, in effect, transferred to the debtor government in exchange for a commitment to spend specified domestic resources on environmental projects. In a recent case in Panama, for example, it was agreed that $30 million of foreign debt would be exchanged for "ecology bonds", the earnings of which would support Government and community projects.

10. Most of the debt in debt-for-nature swaps has been owed to commercial banks, but the Paris Club added a provision to the terms for restructuring the debt owed to official creditors by lower middle-income countries under which such swaps could be arranged. In addition, the Enterprise for the Americas Initiative of the United States of America contains a provision for building environmental funds by using the local currency equivalent of certain interest due to the United States Government. Chile arranged the first swap under this scheme in February 1992. In a multilateral initiative, the Inter-American Development Bank (IDB) allocated $400 million to a Special Financing Modality for Environmental Projects, a pilot programme to assist in debt-for-nature swaps. Under the programme, IDB will lend money to its member countries to purchase commercial debt for environmental purposes.

11. All in all, 1991 was a year of rather modest changes in aggregate debt statistics that broadly continued recent trends and 1992 is expected to continue to follow this pattern. As of mid-year, Mexico recorded a $7 billion reduction in its debt stock through buy-backs and swaps in the secondary market. The conclusion of bank-debt agreements for Argentina and Brazil expected in the second half of 1992 should result in significant debt stock reduction in each case and agreements to restructure the debt owed to government creditors by low-income debtors is further reducing the amounts outstanding, as will be discussed in section III below. In addition, several countries in Africa, Asia and Latin America continue to pursue privatization programmes, many of which involve debt-equity swaps. However, new private and official lending will tend to raise total debt outstanding.

B. Impact on net financial transfers

12. One summary measure of how the debt crisis initially affected developing countries was the net transfer of financial resources that those countries made abroad when foreign banks sharply decreased lending while countries largely maintained their interest payments. In 1991, the capital-importing developing countries received a net financial transfer for the first time since 1982, and the net transfer is likely to remain positive in 1992 as well. The largest changes in 1991 occurred in countries of Latin America and the Caribbean, where the net transfer excluding the flows in and out of official reserves went from a net payment abroad of almost $16 billion in 1990 to an estimated inflow of over $4 billion in 1991, according to the World Economic Survey, 1992. 5/

13. The $20 billion swing in Latin America's net financial transfer seems to have been related to two phenomena. First was progress made and anticipated in regularizing the foreign debt situation in the region and in domestic adjustment programmes. Second was a substantial, speculative inflow that has been attracted by a large interest differential in favour of Latin American countries and a decline in other speculative financial opportunities. As will be discussed in more detail in section III below, the international cash flow changes directly linked to the debt restructuring agreements have been relatively small. The agreements, which are part of packages that include internationally supported adjustment programmes, seem rather to have served as a signal to the financial community.

14. The region of sub-Saharan Africa, where most of the least developed countries are concentrated, continued to receive net financial transfers at about the same nominal level as in earlier years, namely, about $7 billion. Certain amounts of the debt of the low-income countries of this region and others are being written off. However, since much of it was not being serviced in any event and write-offs can lead to a reduction in fresh flows, the immediate cash flow gains to the debtors are expected to be small. As in the case of Latin America, the principal financial gain will be in regularizing international financial relations and, over the long run, stimulating the flows of private funds. In the near term, however, most of these will have to be official flows. Africa has not measurably shared in a surge in direct foreign investment to Asia and Latin America in recent years. Over the long run it must, since direct investment is not only an elastic source of non-debt creating flows, but it can also speed the diversification of Africa's exports into manufacturing.

15. In Asia, where the debt situation has been on the whole more favourable than in Africa or Latin America, the net transfer rose by almost $8 billion last year, mainly because of new credit inflows. In the Republic of Korea, for example, this meant increased borrowing on international markets. In India, in contrast, significant private borrowing in past years rapidly raised debt-servicing, made India vulnerable to a loss of market confidence and required that a stringent process of adjustment be set in motion, which is being supported with increased flows of official credit.

C. Progress in adjustment of heavily indebted countries

16. Many developing countries, particularly heavily indebted ones, continue to undertake internationally supported stabilization and structural adjustment programmes. Rates of progress vary from country to country, although there are certain broad regional features, since some of the determining factors are shared by countries in the same region, such as weather patterns and sometimes political conditions.

17. In Latin America, adjustment and stabilization efforts have increasingly been successful in reducing inflationary pressures and improving fiscal balances, which the interest burden on the debt had helped worsen in the first place. From the beginning, the debt crisis was both a fiscal problem and a foreign-exchange problem, since debt-servicing payments were mainly being paid by Governments. The recent, substantial capital flows to certain countries - a missing link in earlier adjustment programmes - have significantly ameliorated the foreign exchange constraint in those instances, but the pressure to curtail government expenditure and raise taxes remained as before. All in all, the region resumed a positive, though marginal, growth in per capita GDP in 1991 for the first time since 1987.

18. The structural side of the domestic reforms in Latin America and elsewhere aim to reduce market impediments, liberalize trade and shrink the direct role of the state in the economy. In this regard, privatization programmes have gathered momentum in many of these countries. Privatization is considered to have multiple benefits: generating revenue for the Government through sale proceeds and future tax payments, reducing external debt in cases of debt-equity swaps, reducing public expenditure when subsidies can be withdrawn or reduced, inducing investment, and raising efficiency. It has also been increasingly realized, however, that privatization programmes have to be carefully prepared and embody adequate competition so Governments can reap the maximum economic and financial benefits from the sale of public assets.

19. African countries are continuing with economic reform programmes even though the expected improvements in investment and growth have thus far been delayed in many cases. Moreover, some aspects of adjustment programmes, such as large devaluation (Algeria and the Sudan), price liberalization (Egypt and Zimbabwe) and tax rate increases (Togo), have contributed to a rise in inflation. Reduction of excessive budget deficits is being sought through such policies as privatization of state-owned enterprises, increasing tax revenues and reducing government payrolls. The last policy has been especially difficult to implement in some countries that faced direct opposition by civil servants.

20. In many African countries, too little time has passed to assess adequately the progress in adjustment. In others, civil strife and drought have put survival at the forefront of concern. In yet other countries, political reform aimed at greater pluralism has brought changes to the implementation of economic reform programmes.

21. India's major macroeconomic stabilization and structural adjustment programme includes devaluation, liberalization of trade and elimination of traditional subsidies and administered prices. Although the initial effect of the programme is causing inflationary pressure and a privatization programme has faced the opposition of unions, the programme is being broadly supported. Faced with severe budgetary and foreign exchange constraints, Pakistan also launched a major liberalization programme. The measures announced in 1991 include the removal of foreign exchange control, the revision of policies relating to foreign direct investment inflows, banking deregulation and privatization.

22. In Indonesia, a financial deregulation embarked upon in 1988 has resulted in substantial credit inflows that raised external debt by a third in three years. The Government has responded with a mechanism to coordinate international borrowing and has set a ceiling for new foreign borrowing for all public and private borrowers. The country's situation exemplifies the difficulty of carrying out deregulation and the continuing need for a state role in coordinating finance so that a debt burden does not become a debt overhang.

D. Social dimensions of adjustment under debt

23. Economic reforms being implemented in over-indebted countries have had particular social consequences. Stabilization measures follow the basic strategy of reducing demand to redress external and domestic imbalances and naturally have a deflationary aspect, although this stage in adjustment is supposed to be short-term. Structural adjustment programmes are, on the contrary, of medium- and long-term nature, aiming at increasing the economy's productivity and flexibility through liberalization and reallocation of private investment under new market signals and more effective and strengthened public investment programmes. Structural adjustment requires adequate financing for investment and a context of significant economic growth to reabsorb into expanding economic sectors the labour and other resources from shrinking ones. In many cases either the international economic environment or the domestic policy environment, or both, have made it difficult to restart growth, and the social hardships of adjustment have been protracted and multiplied.

24. Low-income groups have been especially vulnerable and their situation has become a focus of international attention. 6/ In more affluent economies, a social safety net, some sort of income insurance, would be provided to assist the poor and unemployed to go through the short-term difficulty. In developing countries, affected individuals have to rely to a much greater degree on activities in the informal sector and on resources of families for their safety net. Yet, the resources of poor families are thin and adjustment has stretched them thinner.

25. Stabilization measures normally include cuts in public expenditure to a far greater degree than increases in revenue. 7/ Cuts are usually made in both current and investment expenditures. When the cuts are short term, postponing investment seems eminently sensible. The difficulty is that infrastructure deteriorates and productivity dips when the cuts are protracted. Human capital and the quality of life suffer when investment is cut in such fundamental areas as education and health. Cuts in current expenditures frequently have severe impacts, especially in urban areas, on low-income people who directly or indirectly lose employment and wages or lose the purchasing power of wages that do not rise as much as inflation, particularly when subsidies on consumer necessities are lost. In a slow-growing environment, such loss of income without alternate opportunities for employment or enterprise has the potential to create a politically volatile situation. That eventuality would only worsen the environment for investment and growth and further drag out the adjustment process.

26. Thus, however much the Government intends to reduce the direct economic role of the state, it is now widely recognized that it must help its people to make the transition during the period of adjustment. The adequacy of safety nets has become a major issue in the design of adjustment programmes. Ghana's Programme of Action to Mitigate the Social Costs of Adjustment was one of the first to target assistance to the victims of certain measures, such as employees of public sector and state enterprises who lost their jobs. In Chile and Morocco, aid was provided to mothers in poor districts and the unemployed in rural areas. 8/

27. However, the fiscal restraints on the government budget make it difficult to implement these measures in most cases. The adjustment programmes were adopted to deal with fiscal imbalances in the first place. Hence, donor governments and multilateral institutions can play an important role in contributing financing, where appropriate, in the form of grants and targeting the assistance on programmes for low-income groups. Indeed, many bodies of the United Nations system have become closely involved in such work. 9/

E. International economic environment

28. In 1991, the volume of Latin America's imports surged by almost 14 per cent. 10/ Import growth had averaged only 5 per cent annually in the previous five years, while before that the large-scale import contractions of the early stages of the debt crisis took place. Latin America's export volume grew an estimated 4.5 per cent in 1991, more than in 1990, but less than in the previous three years. The export volume growth thus did not provide the resources for the increased imports. Indeed, the region's terms of trade fell 6 per cent in 1991 and thus the purchasing power of Latin America's exports did not improve at all. Rather, the import surge was largely financed with much improved net financial transfers to countries of the region. Indeed, net capital inflows to the region were so large that despite the import surge, official reserves rose almost $18 billion.

29. The experience of Africa in 1991 was different. The volume of imports grew less than 3 per cent. After years of decline, imports increased from 1988 to 1990 at an average rate of less than 5 per cent a year. Export volume grew 4 per cent in 1991, but the terms of trade declined by about 7.5 per cent and thus the purchasing power of Africa's exports actually fell. There was no surge in financial inflows in 1991; indeed, the sharp increase in official grants that had been an international response to the economic effects of the crisis situation between Iraq and Kuwait came primarily in 1990. Reserves increased, but by a mere $2 billion.

30. This constraining relationship between trade, debt and finance has been a prominent feature of the developing country debt crisis since the early 1980s. Thus, the sudden relaxation of that constraint in some countries in Latin America in 1991 was most significant. Nevertheless, the surge in the value of imports was especially marked in only a few large countries, such as Mexico, where expenditure on imports rose by a fifth, Argentina, where imports doubled, and Venezuela, where imports rose by almost one half. Even in those countries, however, major concern remains that the higher import capacity be sustained, that it be devoted especially to imports of capital goods, and that the rate of investment and growth rise significantly as well and feed back into the growth of export capacity. In the rest of the debt-constrained developing countries, the primary concern remains what it has been for much of the 1980s, namely, to bring about their own financial turnaround.

31. In this regard, a key question is whether the international economic environment, which has been so difficult for the heavily indebted developing countries generally since the early 1980s, will become more supportive in the 1990s. In one sense it already has. That is, average interest rates charged on developing country foreign debt fell on average, in 1990 and 1991 and they will fall again in 1992. The decline, reflecting declines in average market interest rates, has mainly affected short-term debt and the variable-rate portion of long-term debt, which mainly consists of medium-term loans from commercial banks, excluding several of the instruments that banks have exchanged for their loans in the debt and debt-service reduction agreements that are discussed in section III below. The decline in market interest rates also reduces charges on loans from multilateral financial institutions, albeit with a lag, as these institutions pass on the interest savings on their own borrowing to their debtors.

32. The size of the interest saving arising from the decline in market interest rates depends not only on the portion of debt that carries variable interest rates, but also on the currencies in which the debt is denominated, as interest rates in different markets have followed very different patterns. The London interbank offer rate (LIBOR) on six-month United States dollar deposits, the most common rate to which variable-interest loans are tied, fell from an average of 9.3 per cent in 1989 to 6.1 per cent in 1991, and by June 1992 it had reached 4.1 per cent. But six-month LIBOR rates for deutsche mark loans have risen over the same period. The 1991 average rate of 9.4 per cent was more than double the rate of 1988; by June 1992 the DM LIBOR rate had reached 9.8 per cent. Over the same period, interest rates on loans

in Japanese yen and British pounds sterling first rose and then fell, with the six-month LIBOR rate on yen loans peaking at 7.8 per cent in 1990 and falling to 4.5 per cent by June of this year; pound rates almost reached 15 per cent in 1990 and only slipped below 10 per cent in June of 1992. 11/

33. The World Bank has estimated that such interest rate changes saved the developing countries and transition economies of eastern Europe $13 billion in 1991. 12/ The largest portion of the gain accruing to developing countries was $6 billion in Latin America, where the dollar share of the debt is particularly high. In sub-Saharan Africa, where more of the debt originated in European trade credits, the gain was below $1 billion, with more than a fifth of that accruing to Nigeria.

34. These savings, while significant, must be kept in perspective. First, the gains may be temporary. When economic recovery gathers steam in the United States its interest rates will rise, although the high German rates should recede as soon as the authorities are satisfied with progress in dampening inflation in that country. Moreover, in Latin America where the gains seemed so large, they amounted to less than 4 per cent of export earnings. Indeed, trade is the most important international factor determining the prospects that the heavily indebted developing countries will emerge from their debt crises.

35. The decline in the terms of trade in Africa and Latin America noted above was a reflection of the continued dependence of many of them on traditional commodity exports whose prices fell relative to the prices of the more diversified collection of goods they imported. The international prices of most of these commodities are cyclically sensitive and were affected adversely by the world economic recession of 1991, but the long-run trends in demand also seem to be largely unfavourable. In South and East Asia, in contrast, where manufactures are a larger share of exports, the terms of trade fell only 1.5 per cent in 1991.

36. Countries need to diversify exports into commodities for which the income elasticity of demand is higher and into manufacturing. This should be an investment priority; however, for many countries the key constraint has been that overall investment itself has been grossly inadequate, as domestic and foreign investors have hesitated to commit to substantial new projects.

37. In this regard, there is a lesson in the suddenly increased plans of domestic and foreign investors to build up the export capacity of Mexico. As it is largely in anticipation of the establishment of the North American Free Trade Area, it underlines how important assured market access is to investment plans in the export sector.

38. The uncertainty hanging over the unresolved Uruguay Round of multilateral trade negotiations in the General Agreement on Tariffs and Trade makes it difficult for investors to commit themselves in several product areas. As the experience under the Multi-fibre Arrangement (MFA) showed, when new entrants begin to compete successfully in politically sensitive markets - in this case

in textiles and clothing - importing countries have protected their domestic suppliers by managing the trade, even though doing so contravenes deeply held principles of liberalized trade. A successful Uruguay Round would not only phase out the MFA, but it would also establish stronger rules and disciplines to limit the policy hindrances to trade flows.

39. Most of the investment that must be undertaken in the heavily indebted countries will be in the private sector, but public sector investment is still essential, both for physical and human infrastructure and to act as a catalyst for private investment. The official international community has a traditional role in helping to finance public sector investment in developing countries, as well as in assisting countries through balance-of-payments adjustment. In the latter area, in particular, the ability to continue to lend will finally be ensured through the implementation of the delayed Ninth Quota Increase at the International Monetary Fund (IMF). Assistance for low-income countries is especially important and the recent decision by the IMF Executive Board to extend the Enhanced Structural Adjustment Facility for a year is a positive sign. Most significant, however, are the negotiations currently under way to replenish the funds of the International Development Association (IDA), the highly concessional lending arm of the World Bank. With prospective lending to certain Asian economies in transition, as well as lending for traditional and new environmental projects and programmes, IDA requires a substantial increase in funds.

III. NEGOTIATED DEBT RESTRUCTURING

40. When a private enterprise works itself into an untenable debt situation, unpaid creditors press their claims, the firm defaults, is declared bankrupt and, if efforts of the courts to reorganize the firm fail, the firm's assets are liquidated to make partial payment to the creditors. Governments cannot be liquidated and so creditors must renegotiate insupportable foreign debt burdens with the debtor until the debt overhang is removed. The main aim of the creditors in the negotiation is to collect as much as possible of their outstanding loans and interest; the major fear of the debtor is being cut off from all sources of funds, having to cut back imports severely and to carry out international trade on a cash basis. In the early stages of the debt crisis, several of the debtors' fears were realized, while creditors were largely able to postpone their losses. Over time, creditors increasingly had to face the insolvency of their borrowers, and the international community gradually came to the political judgement that debtors needed to be supported in their economic reform efforts through more debt relief. The degree and modalities of relief nevertheless required negotiation, a process that continues to evolve.

A. Negotiations with international commercial banks

41. With the signing of an outline agreement between the Brazilian Government and its international commercial bank creditors in July of 1992, the heavily indebted developing countries with the largest commercial bank debt have all reached new agreements for "debt and debt-service reduction" (DDSR), as the schemes worked out under the initiative of the United States Secretary of the Treasury have come to be called. Earlier in the year, Nigeria concluded an agreement with its bank creditors in January, the Philippines reached a second phase agreement in February, and Argentina reached an outline agreement in April, which was later finalized in June. 13/ In all, since the Mexican agreement in 1989, there have been nine DDSR cases, involving eight countries, 14/ of which three are still agreements in principle. The agreements cover $150 billion of debt, which is over 30 per cent of the medium-term and long-term bank debt owed by all the capital-importing developing countries taken together.

42. As the latest and most elaborate of the DDSR agreements, the Brazilian case is of some importance. It covers $44 billion in bank claims and took more than a year to negotiate, although it may also be seen as the culmination of several earlier negotiation attempts.

43. The Brazilian menu gives bank creditors the option of exchanging their claims for any of five different bonds at an effective discount of about 35 per cent off face value in each case or lending new money to Brazil. The bonds are structured in different ways to be attractive to banks operating in different regulatory environments and with different preferences for taking on risk to raise their expected returns. One option is to exchange, for example, $100 worth of bank claims for $65 worth of bonds paying market interest rates and maturing in 30 years. In a second option, bank claims would be exchanged at par for 30-year bonds paying below-market interest rates that begin at 4 per cent a year and rise to 6 per cent by the seventh year. The other options are more complicated, entailing different interest rate structures and maturities and varying grace periods. The options also differ in terms of the collateral available to guarantee timely payment.

44. The agreement contains an option for temporary "phase-in" bonds if insufficient resources are available to provide the total collateral for the package of bonds that the creditors choose as a whole. Providing collateral for sovereign-risk loans was an innovation of the DDSR approach, adding an enhancement to the banks to participate in the agreements. As in other cases, it will take the form of purchase by the Brazilian Government of riskless financial instruments, such as zero-coupon United States Treasury bonds, that would be financed out of Brazil's foreign exchange reserves and prospective multilateral credits.

45. The number of options available to the banks in the Brazilian agreement is so large because of the importance given to encouraging the banks to participate without resort to other enforcing mechanisms. Voluntary participation has been an aim of all the internationally negotiated

restructuring of developing country bank debt. It was feared that as private entities with legal claims on debtor Governments, individual banks could take their cases to court if they believed more would be gained thereby than by participating in a concerted debt renegotiation. Court actions in different jurisdictions - each with its own laws, precedents and practices - would likely tie up the resolution of a country's debt problem for many years. However, if banks chose not to participate in a debt renegotiation that succeeded in restoring the debt-servicing capacity of the debtor, it would be a "free rider" if it once again received scheduled payments on its loans without having first shared in the sacrifices of the participating banks. The question for international policy makers was thus how to design a debt-restructuring scheme in which banks would choose to participate and which also accorded significant gains to the debtor country.

46. The DDSR schemes are the latest answer to this question. To see how they work, it is useful to first look at a third option that an individual bank has beside seeking redress in the courts or doing nothing at all. That is, a bank can sell its claim on a debtor country in the secondary market. This market, which originated in banks exchanging claims among themselves on different countries, has operated as well on a cash basis for several years, with the market price expressed as a per cent of the face value of the debt. The bank would sell its claim on a problem debtor at a discount that depended on market sentiment about the country's being able to resume full debt servicing at some later point. As may be seen in figure 2, which shows the average price of the debt of 15 countries that account for almost all the activity in the secondary market (Argentina, Bolivia, Brazil, Chile, Colombia, Côte d'Ivoire, Ecuador, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela and Yugoslavia), the amount of the discount has varied quite dramatically over time.

47. When a market has many buyers and sellers and when there is a large and continuous volume of transactions, the market price is usually an appropriate valuation of what is traded. Although it would be an exaggeration to say that the trading of the bank debt of any country listed on the secondary market is so competitive, the price is said to more or less reflect the present value of the debt servicing that the international financial sector expects the Government will pay over the remaining life of the debt. In other words, a bank that contemplates the secondary market should be indifferent between selling its part of a country's debt at the going price and holding it in return for future debt-service payments.

48. The Government of the debtor country may also have an interest in the secondary market, in this case to retire debt at less than its face value. But because of the nature of the syndication contracts under which most large bank loans were originally made, the cooperation of the creditor banks is generally required for any substantial government buy-back of its debt. All the banks would thus know when a buy-back was in process and this could work to the disadvantage of the debtor Government.

Figure 2. Market bids on bank debt and successor bonds of 15 developing countries, 1986-1992

Source: Department of Economic and Social Development of the United Nations Secretariat, based on data of Salomon Brothers, New York.

49. The reason is that the knowledge that a buy-back is under consideration can reduce the discount. When, as a result of a debt buy-back, the outstanding amount of debt is reduced, the secondary market price could rise due to a higher expectation that the remaining debt will be serviced. 15/ If a bank expects the price to rise after the deal, it will insist on a settlement price at the level where it is expected to be after the reduction occurs, a "post-deal" price. Each bank could always hold onto its part of the debt and wait for other banks to settle the deal at the original price. None would do so and the Government would have to raise its bid to make the purchases.

50. The Bolivian buy-back of March 1988 is a case in point. Bolivia's bank debt had amounted to $670 million, which was valued at $40.2 million in September 1986 prior to the buy-back negotiation, based on a bid price of 6 cents per dollar. In addition, Bolivia had accumulated $300 million in interest arrears. Using funds provided by donor Governments, $308 million of debt together with the interest arrears on that debt were retired at a price of 11 cents to a dollar. The total expense was thus $33.9 million. After the transaction, the remaining $362 million of outstanding bank debt was valued at $39.8 million. The price increase from 6 cents to 11 cents to a dollar of debt meant that even with the face value reduction of almost half of the entire debt stock, the market value of the debt based on the expected payment flow only fell $0.4 million ($40.2 million minus $39.8 million). Since the funds for the buy-back were provided by donors, and perhaps some of them would not have been made available for other uses, Bolivia still made a net gain. The largest portion of the benefit, however, accrued to the banks. Those that sold their claims received more than they otherwise expected and the remaining banks were left with claims that had risen in value. 16/

51. In principle, more of the discount would have been captured by the debtor or its donors if the price of the buy-back had been negotiated directly with all the participating banks at one time in a concerted fashion, rather than leaving banks to sell individually in the market. But such a negotiation would have been extremely time and effort-consuming, as the very different interests of the banks would directly come into play. Some banks with minimal interests in the debtor economy and small lending exposure would have been willing to sell their claims for a lower price than other banks with larger exposures and more extensive business interests there. Banks would also differ in their assessments of the future ability of the country to service the debt. There could thus be quite a range of the lowest price that each bank would accept, called its "reservation price". If all the banks were to participate and no banks were to make a loss, the operation would have to settle at the highest reservation price. In that sense, all banks would sell their claims at the price that the bank that was least willing to part with its claims insisted upon.

52. Although concerted debt sales of this sort did not take place, a comparable dynamic characterized the negotiations for concerted debt restructuring in the 1982-1988 period that preceded the current DDSR menu approach. There, instead of jointly accepting a selling price for their claims, banks had to agree to a single revised schedule of debt servicing and joint provision of new loans to help finance that debt servicing. The increasingly disparate interests of the banks made it more and more difficult to reach agreement in successive rounds of debt rescheduling.

53. One key advance in the new DDSR approach was that participating banks could choose different options. There is no single price on which all have to agree, no single debt rescheduling and refinancing package that all have to adopt. DDSR agreements are formed in two stages: first, a menu of options and their pricing are negotiated; and second, the creditors commit themselves to the various options. As in the Brazilian agreement noted above, the

options normally include swapping bank claims for bonds with less face value or for bonds at par but with lower interest rates, or retaining bank claims but lending new money to help service the debt while increasing the individual bank's exposure. Sometimes they also include a cash buy-back at a specified discount price. The prices and terms of the replacement financial instruments are negotiated with an eye on the secondary market and expectations about the participating banks' reservation prices. The banks then make their choices depending in part on the regulatory environment they face. 17/

54. The banks that choose one of the bond swaps or the cash sale thereby recognize formally that their bank loans have less than face value and they thus take an accounting loss if they had not already done so at the insistence of their regulatory agencies. All the other banks, that is, those that have a higher reservation price than the price in a cash buy-back or the price implicit in the various bond swaps, choose the new money option. If their regulatory agencies are accommodating, those banks do not have to show an accounting loss; but they incur an implicit loss, known as the "new-money tax", because from the first moment their new loans are issued they will trade on the secondary market at the same discount as the outstanding old debt. 18/

55. If banks were completely free to choose among the menu options, they might also be free not to participate at all. Such banks would still benefit from the rise in the post-deal price of the debt in the secondary market. Mechanisms were thus needed to prevent free riding. The most notable is the "novation" clause. For example, the Mexican agreement of 1989 stated that the conversion of outstanding debt into new instruments constituted a new contract, supplanting the old one. This meant that a bank holding an old debt claim but refusing to exchange into one of the new instruments would have a lower priority in receiving payments from Mexico.

56. The results of the five DDSR agreements that were completed before the end of 1991 are shown in table 2. The agreements differed very significantly in the effective degree of debt reduction accorded to the debtor Governments. 19/ The table shows the debt-reduction equivalent of the easier terms of debt servicing plus the actual debt reduction agreed for each country. It also shows additions to each country's debt from new official loans planned specifically for purchasing enhancements to the debt instruments and the new money loans extended by the banks that took the new-money option, which were quite small relative to the debt and debt service reduction, except for the Philippines. Taken together, these items give the net debt reduction shown in the table. It is a generous measure of the net benefit of each agreement, as it excludes each country's use of its own reserves and already planned borrowing from multilateral institutions that were co-opted for debt enhancement purposes. In any event, measured this way, the total debt of Costa Rica fell $1 billion or slightly more than one fifth of its $4.6 billion debt before the agreement. As a percentage of total debt, this was the largest gain, while that of the Philippines - or more properly, phase I of the Philippines' two-part negotiation - was the smallest, as its debt fell only 2 per cent. The debt of Uruguay was brought down quite significantly, that of Mexico and Venezuela by smaller degrees.

Table 2. Results of agreements to reduce foreign bank debt of five developing countries a/

(Billions of United States dollars)

	Mexico	Philippines	Costa Rica	Venezuela	Uruguay
Pre-agreement debt (face value)					
Total	95.4	28.5	4.6	32.5	3.7
Eligible bank debt	47.2	6.6	1.6	19.0	1.6
Present value of debt reduction when deal made					
Debt and debt-service reduction agreed	14.2	1.3	1.1	4.4	0.8
Associated additional debt					
Official enhancements	3.7	0.1	0.2	0.7	0.1
"New money" from banks	1.0	0.7	-	1.2	0.1
Net debt reduction b/	9.4	0.5	1.0	2.6	0.6
Market value of eligible bank debt					
Pre-deal	17.0	2.6	0.2	7.0	0.9
Post-deal c/	17.7	3.1	0.2	9.6	0.7
Memorandum item					
Secondary market prices (per cent of face value)					
Pre-deal	36	40	12	37	56
Post-deal d/	52	52	39	61	74
Agreement equivalent e/	41	46	24	50	60

Source: Department of Economic and Social Development of the United Nations Secretariat, based on estimates of Stijn Claessens, Ishac Diwan and Eduardo Fernandez-Arias, "Recent experience with commercial bank debt reduction", World Bank, 1992.

a/ Countries having completed debt and debt-service reduction agreements by end-1991 (Philippines refers to phase I agreement).

b/ Calculation does not take account of official loans that would have been extended in any event but that were set aside for purposes of the agreement and thus were unavailable for other uses; nor does it include use of the country's own reserves for enhancements.

c/ Post-agreement debt as if all of it had the same debt-servicing schedule as pre-agreement debt (thus, excluding increase in market price from enhancements, but including new money at market price).

d/ Excluding increase in price associated with collateral and interest guarantee enhancements.

e/ Full market value of new claims minus face value of new money provided, expressed as a percentage of face value of eligible debt.

/...

57. The agreements were more similar, however, in the degree to which they were able to capture the discount on the debt for the debtor country. To measure this factor requires calculating an implicit secondary market price for a buy-back that would be equivalent to the negotiated DDSR package. The implicit buy-back price is calculated as the total market value of newly created bank and bond claims except for the new money loans, divided by the face value of eligible commercial bank debt. The numerator shows, in effect, the value at which old debt was exchanged in the deal. The expression as a whole thus shows the implicit average discount of the DDSR.

58. As expected, the post-deal price was higher than the pre-deal price in all the DDSR agreements. Had the negotiations followed the earlier concerted approach without a menu of options for the creditors, the settlement price would have had to be relatively close to the post-deal price to accommodate the banks with the highest reservation prices, if all the banks were to be included without any discrimination. However, the pre-deal price set a floor to the settlement price if no banks were to see themselves worse off after the deal than before it. Table 2 shows that the implicit agreement price was generally about half way between the post-deal and pre-deal prices, although the Mexican and Uruguayan settlements were closer to the pre-deal prices. Therefore, each of the deals shows some features of a concerted agreement with some degree of discrimination among the different interests of the creditor banks.

59. There is a sense, however, in which these countries were victims of the success of their agreements. As noted above, the post-deal prices were higher than pre-deal prices in all cases, indicating the financial markets' assessment that the debt-servicing capacity of the countries had risen. If the market is correct, then the debt-servicing flow from the post-deal debt is expected to be quite close to the debt-servicing flow that the country would have paid on the larger outstanding debt before the deal. In all cases except that of Uruguay, the post-deal debt level exceeds the pre-deal level, indicating that the market expects more debt servicing to be paid on the remaining debt than would have been paid before, although the differences are not large. And in all the cases, the calculation excludes the effect of having added to official debt to finance the enhancements to the bank debt.

60. In other words, the expected debt-servicing cash flow after the DDSR agreements is not very different and in most cases even larger than it was before the agreement was reached. This is not necessarily a bad result. First, because it is a voluntary scheme - the only type that policy makers countenanced - the banks were not expected to accept a situation that they perceived to be worse than the one they saw themselves in before the deal was made. Second, in some cases the pre-deal expectation of debt servicing was very much affected by the growth of arrears on interest as well as principal payments. The agreements essentially validated what the Governments and the markets had been saying, namely, the countries could not and would not service the outstanding claims against them. Arrears signalled this fact in a sometimes dramatic and sometimes quiet way. 20/ But arrears were never intended to be a solution to the debt problem.

B. Negotiations with official creditors

61. It might be assumed that all the careful crafting of incentives and penalties to encourage banks to participate voluntarily in multilateral debt restructuring exercises would be unnecessary when it came to designing policy for restructuring debt owed to official creditors. In fact, however, discussions among major creditor countries on terms for restructuring intergovernmental debt have been protracted and difficult and the concessions accorded to the debtors have until recently been quite modest. Every year since 1983, from 15 to 24 developing countries have rescheduled their debt through the Paris Club, most in a sequence of relatively short-term agreements. 21/

62. Indeed, creditor participants in the Paris Club often seem to act more like representatives of financial enterprises than Governments. The analogy is not complete. The primary obligation of managers of commercial banks is to make profits for their shareholders. The primary aim of creditor representatives in the Paris Club seems to be to minimize financial losses of their Governments. Although Paris Club negotiations embrace direct government loans, including official development assistance (ODA) credits, much of the portfolio of claims consists of export credits that their Governments guaranteed and on which the debtor defaulted. There is an especially strong incentive to collect on these loans. The reason is what analysts call "moral hazard" and means that the last thing a guarantee agency wants is for borrowers to believe that default is not difficult and expensive. 22/

63. It is thus not surprising that the Paris Club insisted on only rescheduling loans - and on commercial terms - long after commercial banks were recognizing the need to forego permanently some debt servicing by the same borrowers. Commercial bankers regret losses and try to avoid them, but will turn their attention to other activities in search of profits rather than dwell indefinitely on collecting on the losses. In the terminology of the previous section, they have lower "reservation prices" than Paris Club creditors.

64. Sometimes, however, it appears that normal negotiating goals in the Paris Club are superseded. It is, after all, an intergovernmental forum and Governments can choose it as a vehicle for foreign policy. Financial transfers are among the most common tools of policy and foreign indebtedness, particularly of poor countries to rich countries, has high political visibility. Thus, unlike bank presidents who would be hard pressed to explain losses to their boards of directors, heads of Government could extend financial concessions to foreign Governments as a political gesture. Accepting the foreign policy, legislators would approve the gesture and voters would accept it.

65. The relevance of this distinction was made most clear in 1991 when, quickly breaking with painstakingly negotiated terms for multilateral relief of official debt-servicing obligations, the industrial countries offered far deeper debt-relief concessions to Egypt and Poland than they had made

available to the poorest nations in the world. The political importance of extending major financial assistance to these two nations was manifest at the time: the first as part of the global coalition to undo Iraq's occupation of Kuwait and the second as support for a leading edge of the economic and political revolution that swept across eastern Europe and the former Union of Soviet Socialist Republics.

66. In earlier years, Paris Club representatives had argued that the proper mechanism for multilateral official assistance to countries lay elsewhere, in aid consortia. 23/ The Paris Club was supposed to help Governments through temporary liquidity difficulties. But as the commercial banks came to realize, several countries had become insolvent. In agreeing to accord a measure of debt reduction to low-income countries, Paris Club creditors also acknowledged that neither these debtor Governments nor their aid agencies in the creditor countries could or would allocate the resources from their budgets year in and year out to fully service their credits.

67. The approach the Paris Club eventually took to improving the terms of debt restructuring bears some similarity to that taken in the current international strategy on commercial bank debt. Thus, in order to gain the advantages of a concerted agreement with discrimination among creditors - to take advantage of the creditors' different "reservation prices" - the Paris Club has offered its members a menu of restructuring options in the treatment of the debt of selected countries. In comparison with the DDSR agreements, however, the menu is largely pre-set and the variables left to negotiation are quite limited.

68. Whereas the major industrialized countries insisted upon a case-by-case approach in which each debtor Government negotiated a package with a committee representing all its commercial banks, the Paris Club creditors first negotiated among themselves the basic terms of relief they would apply to specified groups of countries and then decided for which set of terms individual countries were eligible. The only exceptions are ones in which political considerations predominated, as in the cases of Egypt and Poland, and in the agreement for Peru in 1991, in which debt that is usually ineligible for rescheduling was included in the package as part of the international effort to assist the new Peruvian Government to re-establish effective working relations with the multilateral financial community.

69. The most concessional of the three standard treatments currently available from the Paris Club has been named the "enhanced concessional treatment for the poorest and most indebted countries". 24/ The new terms have been available since the end of last year and as of mid-1992, six countries have benefited from them: Benin, Bolivia, Nicaragua, Togo, Uganda and the United Republic of Tanzania. 25/

70. Calculations for a debtor country under the enhanced terms begin by looking at the scheduled debt servicing of eligible non-concessional debt over a set period, the "consolidation period", which might be one to three years long. The analysis estimates what that payment stream would be worth

today, its "net present value". 26/ The menu then offers three ways to give relief so as to halve this amount plus accumulated arrears. Creditors can choose to write off half the total and reschedule the rest with a new loan repayable over 23 years (with a six-year grace period) paying market interest rates, or creditors can either reschedule the entire amount over 23 years at a concessional interest rate or choose a particular combination of the two approaches, as long as the result would be financially the same in the sense of halving the total present value. ODA debt will be rescheduled over 30 years, with no principal due for 12 years and at an interest rate at least as favourable as the original one.

71. However, certain creditors have not agreed to grant the enhanced concessional terms and the Club is allowing them to apply the treatment they used before for low-income countries (the "Toronto terms"). This requires that the arrears plus debt-servicing due during the consolidation period be rescheduled over 25 years at market interest rates, with no principal due for 14 years. These terms are meant for the creditor Governments with the higher "reservation prices". It gives no reduction in net present value, but it gives an unusually long grace period.

72. The Paris Club's second treatment is the "Houston terms", named after the 1990 summit meeting of the seven major industrialized countries in which special treatment was proposed for lower-middle income countries. These terms give no reduction in present value, no write-off of any of the debt. Rather, debt servicing during the consolidation period is rescheduled over 15 years with an 8-year grace period for non-concessional debt and 20 years with a 10-year grace period for ODA debt. In addition, a part of the debt can be swapped in debt-for-nature, debt-for-aid, debt-for-equity or other local currency uses, an option that is now also extended to low-income countries.

73. Finally, for developing countries that do not fall into either special category, the standard Paris Club terms apply, namely, debt-servicing due during the consolidation period is rescheduled over 10 years with a 5-year grace period on principal payments, although Brazil was accorded a maturity of 13.5 years in its agreement this year.

74. It has been standard practice in Paris Club agreements to reschedule debt servicing in a sequence of "consolidation periods", whose average length rose only from 1 to 1.5 years in the 1980s. Except for the cases of Egypt and Poland, which included all the debt servicing due on all the eligible debt, the consolidation periods in agreements signed in the 1990s are not being extended more than a year or so beyond earlier practice. The individual agreements are thus not expected to resolve completely all official debt-servicing difficulties, unlike the DDSR agreements which are meant to be the final round in commercial bank rescheduling.

75. There is a requirement under the Paris Club that debtors undergo an internationally supported adjustment programme, and the repeated returns to the Club for new agreements give a mechanism for continued linking of debt restructuring and adjustment policy. The consequence has been, however, that

debtor government officials are spending inordinate amounts of time renegotiating their debt, beginning one Paris Club round as another finishes. 27/ In this regard, one clause in the new, enhanced treatment for low-income countries holds out an interesting possibility, as it specifies that the creditors would consider "the matter of the stock of debt" after a period of three or four years. This means that an agreement might then be negotiated covering the entire outstanding stock of debt, as has become a common practice in the restructuring of commercial bank debt.

IV. CONCLUSIONS

76. After a decade of international debt crisis, the outlook is finally improving, in particular, for the middle income countries. The net transfer of financial resources has turned positive on the strength of private flows to several of the largest heavily indebted countries, but the net transfer of financial resources to low-income countries remains stagnant. Official as well as private creditors have acknowledged the existence of a debt overhang requiring debt reduction in various circumstances. Domestic adjustment has prepared the ground for more sustainable growth in many developing countries.

77. It is necessary, however, not to let the desire for release from the international debt crisis cloud the perceptions of what has and has not yet been accomplished. In the arena of debt negotiations itself, there is now a greater variety of policy tools, menus and treatments than ever before available to debt negotiators. The number of countries to have benefited from the new terms, however, remains quite limited. Indeed, the countries that have not yet settled their debt-servicing arrangements need to be alert to the full range of options utilized in other cases and the possibilities for additional "financial engineering". Considerable work thus remains in the international debt policy arena.

78. Moreover, there is no formal mechanism to restructure the debt owed to multilateral creditors. 28/ When countries cannot service such debt on a timely basis, they accumulate arrears. Ten countries had obligations overdue six months or more to the IMF that totalled $4.5 billion at the end of fiscal year 1991/92, which was more than 12 per cent of total Fund credit and loans outstanding. This was despite efforts, particularly on the part of four countries, to settle obligations as they fall due and undertake adjustment programmes that could lead to the settlement of their arrears. At the World Bank, six countries were in non-accrual status due to their outstanding arrears at the end of fiscal 1991/92. They accounted for 2 per cent of the Bank's outstanding loans, an improvement over the previous year when eight countries were in non-accrual status and owed 3 per cent of the Bank's loans. 29/ This is especially important as the IMF, the World Bank and the regional development banks have increasingly become the chief sources of credit for many countries. The severely indebted low-income countries already paid a third of their debt servicing to these institutions in 1990; it was under one fifth in 1980. 30/

79. It is not yet clear if the DDSR debt agreements will end the cycles of debt negotiations for the participating countries, which they are supposed to do. They have indeed raised expectations in the financial community about the future debt-servicing prospects of the heavily indebted middle-income countries. But the new debt instruments do not yet trade in the secondary market at par; i.e., the market still sees a significant possibility of debt-servicing difficulties ahead. If they emerge, the situation will indeed be difficult, since it is not clear how a debt restructuring with private creditors could be negotiated, if at all, with a large, dispersed number of bondholders. In this regard, the risk seems to have been passed to the official creditors.

80. Finally, a substantial part of the new capital inflows to the heavily indebted countries appears to be highly speculative funds. Financial markets in some of these countries have burgeoned, while remaining extremely volatile. Moreover, the countries that regained market access are none the less considered high-risk credits and their borrowing instruments entail interest premiums, significant collateral or other special arrangements. Especially since the net international cash flow from debt agreements did not improve in the cases of the countries most indebted to foreign commercial banks, the quantity and quality of new flows is extremely important. Indeed, it is a concern that the inflow of funds has only to a limited degree thus far found its way into higher aggregate investment in new plant and equipment and the rate of growth of output has remained sluggish.

Notes

1/ Additional details and related analyses may be found in concurrent reports prepared for the Assembly on the net transfer of resources of developing countries (A/47/404), and on the implementation of the International Development Strategy for the Fourth United Nations Development Decade (A/47/270) and on the Declaration on International Economic Cooperation, in particular the Revitalization of Economic Growth and Development of the Developing Countries (A/47/377).

2/ For the definition of capital-importing developing countries, see World Economic Survey, 1992 (United Nations publication, Sales No. E.92.II.C.1).

3/ For statistical purposes, the region is defined to exclude Nigeria and South Africa.

4/ Swaps to support other assistance programmes have also continued; for example, Harvard University arranged a debt-for-education swap for Mexico in 1991, after having made a similar arrangement for Ecuador in 1990.

5/ United Nations publication, Sales No. E.92.II.C.1, p. 217.

Notes (continued)

6/ The work that most galvanized world opinion on this was Andrea Cornia, Richard Jolly and Francis Stewart, Adjustment with a Human Face, 2 vols. (New York: Oxford University Press for UNICEF, 1987). A continuing need to focus on the issue is argued, for example, in the report of the Committee for Development Planning on its twenty-eighth session, Official Records of the Economic and Social Council, 1992, Supplement No. 7 (E/1992/27), paras. 155-161.

7/ See World Economic Outlook (Washington, D.C.: IMF, May 1992), pp. 23-25 and 72-77.

8/ On these and other cases, see Christian Morrison, ed., Adjustment and Equity in Developing Countries, 8 vols. (Paris: Organisation for Economic Cooperation and Development, 1992).

9/ See "Policies and activities relating to assistance in the eradication of poverty and support to vulnerable groups, including assistance during the implementation of structural adjustment programmes", report of the Secretary-General (E/1992/47), paras. 66-73.

10/ Data and estimates for Latin America and Africa in this section are drawn from the World Economic Survey, 1992.

11/ Based on data of IMF, International Financial Statistics, August 1992.

12/ See Global Economic Prospects and the Developing Countries (Washington, D.C.: World Bank, April 1992), p. 9.

13/ These were described in World Economic Survey, 1992, pp. 77-79.

14/ Argentina, Brazil, Costa Rica, Mexico, Nigeria, Philippines (phases I and II), Uruguay and Venezuela. The possibility of a DDSR arrangement was agreed by Morocco and its bank creditors in September 1990 as a follow-up to a conventional rescheduling at that time. In addition, Chile and its bankers agreed to a rescheduling in December 1990 that had a voluntary "new-money" feature that is in the spirit of the DDSR agreements.

15/ The main case in which the price would not rise is when the Government undertakes the buy-back with its own reserves, which would have otherwise served as informal collateral and earned interest (for a formal analysis of buy-backs, see Michael P. Dooley, "Buy-backs, debt-equity swaps, asset exchanges, and market prices of external debt", in Jacob Frenkel, Michael Dooley and Peter Wickham, eds., Analytical Issues in Debt (Washington, D.C.: International Monetary Fund, 1989), pp. 130-150).

Notes (continued)

16/ For a fuller discussion, see Jeremy Bulow and Kenneth Rogoff, "The buy-back boondoggle" and Jeffrey Sachs, "Comprehensive debt retirement: the Bolivian example" and associated commentary in Brookings Papers on Economic Activity, 1988, No. 2, pp. 675-715.

17/ On the latter, see United Nations Centre on Transnational Corporations, Transnational Banks and the External Indebtedness of Developing Countries: Impact of Regulatory Changes (United Nations publication, Sales No. E.92.II.A.10).

18/ Nevertheless, the market value of their old claims rises if the post-deal price exceeds the pre-deal price, which is the expected case. The point is that by extending new money loans, the reluctant banks are not completely free riders.

19/ The analysis and calculations presented here are drawn from Stijn Claessens, Ishac Diwan and Eduardo Fernandez-Arias, "Recent experience with commercial bank debt reduction", World Bank Policy, Research and External Affairs Working Paper, forthcoming.

20/ See Oscar Altimir and Robert Devlin, "An overview on debt moratoria in Latin America", Economic Commission for Latin America and the Caribbean, Working Paper No. 6 (June 1992).

21/ See World Economic Survey, 1992, p. 228.

22/ This can be contrasted with the treatment of ODA debt; i.e., over $11 billion of ODA debt owed by poorer developing countries have been unilaterally cancelled by the donors, initially under an agreement in UNCTAD (Trade and Development Board resolution 165 (S-IX) of 11 March 1978) and subsequently under the initiative of individual donors (data as reported by donors through October 1991; see World Bank, World Debt Tables, 1991-92 (Washington, D.C.: World Bank, December 1991), p. 27).

23/ See the discussion in World Bank, World Debt Tables, 1991-92, p. 66.

24/ This treatment resulted from a proposal made by the United Kingdom at a Commonwealth Finance Ministers' meeting in Trinidad and Tobago which, while not being adopted by the major creditor Governments, led to an agreement at the 1991 London Summit of the seven major industrial countries to improve upon the restructuring terms then available to low-income countries.

25/ The following discussion of Paris Club debt is largely based on material prepared in the UNCTAD secretariat for the 1992 Trade and Development Report.

Notes (continued)

26/ Net present value can be thought of as the amount of cash that the creditor would find equivalent to the assured stream of debt-servicing payments contracted. The calculation in this case takes no account of the possibility that the debtor will be unable to make all payments in a timely manner.

27/ The Paris Club process requires first that an "agreed minute" be negotiated between the debtor and the creditors meeting together and that the debtor then negotiate detailed bilateral agreements to implement the minute with each creditor.

28/ A programme has been developed to assist countries in arrears to the IMF to work down the arrears and accumulate rights to draw on the Fund as soon as the country returns to normal membership status; a parallel programme applies to arrears to the World Bank (see World Economic Survey, 1991, pp. 157-158).

29/ Based on information provided by IMF and World Bank.

30/ Data of World Bank, World Tables (see also G. K. Helleiner, "The IMF, the World Bank and Africa's adjustment and external debt problems: an unofficial view", World Development, vol. 20, No. 6 (June 1992), pp. 779-792).